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Abstract

The subject of this speech is how to improve enforcement of Europe's ban on abuse of monopoly power. This ban is laid down in Article 82 of the Treaty Establishing the European Community ("EC Treaty"), our equivalent of Section 2 of the Sherman Act in the United States. Such enforcement is a crucially important element in ensuring an effective competition policy, which is in turn a key factor in increasing Europe's competitiveness.

SPEECH

TACKLING EXCLUSIONARY PRACTICES TO AVOID EXPLOITATION OF MARKET POWER: SOME PRELIMINARY THOUGHTS ON THE POLICY REVIEW OF ARTICLE 82

*Neelie Kroes**

Ladies and gentlemen, it is a great pleasure and honor for me to address this long-established international antitrust forum that has always taken such a welcome and keen interest in the development and application of European competition policy.

The subject of my speech today is to how to improve enforcement of Europe's ban on abuse of monopoly power. This ban is laid down in Article 82 of the Treaty Establishing the European Community ("EC Treaty"),[1] our equivalent of Section 2 of the Sherman Act in the United States.[2] Such enforcement is a crucially important element in ensuring an effective competition policy, which is in turn a key factor in increasing Europe's competitiveness.

I. *ARTICLE 82*

Article 82 deals with unilateral conduct by an enterprise with market power, which restricts competition on the market.[3] I am convinced that the exercise of market power must be assessed essentially on the basis of its effect in the market, although there are exceptions such as the per se illegality of horizontal price fixing.[4] This is consistent with the way we apply Europe's rules on collusive behavior, laid down in Article 81 of the

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1. Consolidated Version of the Treaty Establishing the European Community art. 82, O.J. C 325/33, at 65 (2002) [hereinafter EC Treaty].

2. Sherman Act, 15 U.S.C. § 2 (2000).

3. *See* EC Treaty, *supra* note 1, art. 82, O.J. C 325/33, at 65 (2002).

4. *See id.* at 64-65.

EC Treaty, as well as other instruments of European competition law.

Ladies and gentlemen, I would like to emphasize that it is not our intention to propose a radical shift in enforcement policy. We simply want to develop and explain theories of harm on the basis of a sound economic assessment for the most frequent types of abusive behavior to make it easier to understand our policy, not only as stated in policy papers, but also in individual decisions based on Article 82.

Article 82 enforcement should focus on real competition problems: In other words, behavior that has actual or likely restrictive effects on the market, which harms consumers. There are two main reasons for this: Firstly, enforcement agencies should be cautious about intervening in the functioning of markets *unless* there is *clear* evidence that they are not functioning well. As you say in the United States, "if it ain't broke, don't fix it!" Secondly, enforcement agencies do not have unlimited resources and need to focus their efforts on what makes a real difference.

As I am sure you all know, I am an economist by training. Now I am an antitrust enforcer by profession! As an economist, I want an economically sound framework. But as an enforcer, I need a workable and operational tool for making enforcement decisions.

It is not the aim of the current review to end enforcement of Article 82. Any conclusions we reach on the right economic approach to adopt must take into account the need to ensure that the rules can be enforced effectively.

II. *DOMINANCE*

Article 82 only applies to companies in a dominant market position, and naturally I identify dominance with substantial market power.

In order to conclude that a company has substantial market power, one must conduct a detailed analysis of key issues, such as the market position of the allegedly dominant company, the market position of competitors, barriers to expansion and entry, and the market position of buyers. This means that I consider that high market shares are not, on their own, sufficient to conclude that a dominant position exists. Market share presump-

tions can result in an excessive focus on establishing the exact market shares of the various market participants. A pure market share focus risks failing to take proper account of the degree to which competitors can constrain the behavior of the allegedly dominant company. That is not to say that market shares have no significance. They may provide an indication of dominance—and sometimes a very strong indication—but in the end a full economic analysis of the overall situation is necessary.

III. *THE CONCEPT OF ABUSE*

In our view, the objective of Article 82 is the protection of competition on the market as a means of enhancing consumer welfare and ensuring an efficient allocation of resources.

We also think that it is sound for our enforcement policy to give priority to so-called exclusionary abuses, since exclusion is often at the basis of later exploitation of customers. I will therefore focus on exclusionary abuses and will not deal with what we call exploitative abuses, such as, for instance, excessive pricing; nor will I deal with discriminatory abuses. This being said, I am well aware that some abuses may have effects, which both exclude and exploit or discriminate. I will deal with exploitative abuses in a second round of our policy review.

Some may think it is somewhat surprising that after many years of enforcement against abusive conduct there is still a lively debate on the objectives of Article 82.[5] Indeed, there is a similar debate about Section 2 of the Sherman Act here in the United States.[6]

I am aware that it is often suggested that—unlike Section 2 of the Sherman Act—Article 82 is intrinsically concerned with "fairness" and therefore not focused primarily on consumer welfare.[7] As far as I am concerned, I think that competition policy

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5. *See* COMPETITION LAW OF THE EUROPEAN COMMUNITY § 3.02 (Valentine Korah ed., 2005) (noting that the precise role of Article 82, and its relationship with other objectives of the European Union and the policy underlying it, have not yet been settled definitively).

6. *See* A CENTURY OF THE SHERMAN ACT: AMERICAN ECONOMIC OPINION, 1890-1990 (Jack C. High & Wayne E. Gable eds., 1992) (collecting articles documenting the shifting objectives of Sherman Act); *see also* Rudolph J. R. Peritz, COMPETITION POLICY IN AMERICA: HISTORY, RHETORIC, LAW (rev. ed. 2000) (recounting history and evolution of Sherman Act).

7. *Compare* Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 767 (1984) (stating that aggressive competition, though perhaps unfair to less efficient busi-

evolves as our understanding of economics evolves. In days gone by, "fairness" played a prominent role in Section 2 enforcement in a way that is no longer the case.[8] I don't see why a similar development could no take place in Europe.

My own philosophy on this is fairly simple. First, it is competition, and not competitors, that is to be protected. Second, ultimately the aim is to avoid consumer harm.

I like aggressive competition—including by dominant companies—and I don't care if it may hurt competitors, as long as it ultimately benefits consumers. That is because the main and ultimate objective of Article 82 is to protect consumers,[9] and this does, of course, require the protection of an undistorted competitive process on the market.

We need to take into account not only short-term harm, but also medium and long-term harm arising from the exclusion of competitors. I am well aware of the difficulty associated with predicting medium or long-term harm. But I believe that we should focus not only on, for instance, the short-term price effects of a certain form of conduct, but also take into account the medium to long-term effects should residual competitors be foreclosed. Consumer prices may fall in the short-run but end up being higher in the medium to long-term because of the likely foreclosure effects. We cannot just wash our hands of responsibility and say that competition law cannot or should not protect the consumer against negative medium to long-term effects, just because it is difficult to assess.

The judgment of the European Court of Justice in the *Hoff-*

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nesses, "is precisely the sort of competition that promotes the consumer interests that the Sherman Act aims to foster"), *with* British Airways PLC v. Commission, Case T-219/99, [2003] E.C.R. II-5917, __, ¶ 242, [2003] 4 C.M.L.R. 19, 1050-51 ("[W]hilst the finding that a dominant position exists does not in itself imply any reproach to the undertaking concerned, [the dominant undertaking] has a special responsibility, irrespective of the causes of that position, not to allow its conduct to impair genuine undistorted competition on the common market.").

8. *See* Eleanor M. Fox, *Monopolization and Dominance in the United States and the European Community: Efficiency, Opportunity, and Fairness*, 61 NOTRE DAME L. REV. 981, 981-84 (1986).

9. *See, e.g.*, Microsoft v. Commission, Case T-201/04, [2005] E.C.R. __, __, ¶ 150, [2005] 4 C.M.L.R. 5, 450 (stating that "the purpose of [EC Treaty Article 82] is to safeguard the interests of consumers, rather than to protect the position of particular competitors") (internal quotations omitted).

mann-La Roche case[10] is a good starting point to define abuses that exclude. The Court emphasized that the behavior under review has to have a certain effect on the market.[11] Second, the Court values the protection of equal opportunities for residual competition, so that remaining competitors are able to improve in efficiency and thereby increase competition to the dominant company.[12] This means two things: Firstly—the conduct of the dominant firm must have the *potential* to influence the position of residual competition on the market and therefore be likely to negatively impact prices, quantities or innovation in the market. In other words what we call "foreclosure." Secondly—a market distorting foreclosure effect must be established and not simply the foreclosure of one or two competitors. This may depend on factors such as the market coverage of the conduct or, for example, the selective nature of the conduct if it targets strategic customers that may be important for new entrants or residual competitors. These factors must be analyzed to check whether there is a credible "theory of foreclosure" that fits the facts of the case.

IV. *PRICE BASED ABUSES*

A famous phrase in the *Hoffman-La Roche* judgment is "through recourse to methods different from those which condition normal competition."[13] This is, of course, connected to the well-known issue of what constitutes "competition on the merits," and is a particularly controversial subject with respect to price-based abuses—especially rebates. I would like to spend a moment on how one could think about this.

Exclusionary abuses may be both price based and non-price based: Examples of non-price based abuses, where it is clear that some 'exclusion' takes place, are contractual tying, "naked" refusals to supply, and single-branding obligations (which you in the United States call exclusive dealing).[14] The question is whether such exclusion may be characterized as anticompetitive,

10. *See* Hoffman-La Roche & Co. AG v. Commission, Case 85/76, [1979] E.C.R. 461, [1979] 3 C.M.L.R. 211.

11. *See id.* at 467, [1979] 3 C.M.L.R. at 219-20.

12. *See id.* at 578-80, [1979] 3 C.M.L.R. at 239-41.

13. *Id.* at 540, [1979] 3 C.M.L.R. at 232.

14. Commission Notice, O.J. C 291/1, at 21 (2000) (Guidelines on Vertical Restraints).

in other words, impacting not only competitors, but also competition in the market.

Similar exclusionary effects may be achieved through pricing. For instance: very high stand-alone prices in comparison to a low bundled price for two products may "tie" these two products together as effectively as contractual tying; asking a very high price for a product or combining a high upstream price with a low downstream price may amount to a "constructive" refusal to supply; high rebates given on condition of single branding may have the same effect as contractual non-compete obligations; last but not least, predatory pricing is, of course, meant to exclude competitors.

However, low prices and rebates are normally to be welcomed, as they are beneficial to consumers. So how do we decide what should properly be regarded as "competition on the merits" when it comes to price based conduct?

Certain forms of pricing conduct may have different exclusionary effects depending on how efficient the rivals are. It is clear to me that inefficient competitors should not be protected by competition policy from aggressive price-based actions of a dominant firm. In my view, "competition on the merits" takes place when an efficient competitor that does not have the benefit of a dominant position, is able to compete against the pricing conduct of the dominant company.

One possible approach to pricing abuses could be based on the premise that only the exclusion of "equally efficient" competitors is abusive. The benchmark for "as efficient" would normally be the costs of the dominant company, except where it is not possible to determine such costs, or when the dominant company—for instance in a newly liberalized market—has some "first-mover advantages" that later entrants cannot be expected to match.

V. *EFFICIENCIES*

Another widely debated issue is whether it is desirable and indeed possible for there to be an "efficiency defense" under Article 82.

Article 82 does not expressly foresee the possibility of "exempting" abusive behavior because of efficiencies. However, we must find a way to include efficiencies in our analysis. We must

take into account that the same type of conduct can have efficiency-enhancing as well as foreclosure effects. This should be reflected in our analytical framework.

I have to admit it is difficult to explain why we consider efficiencies under Article 81 and under the Merger Regulation, but not under Article 82. At the most basic level, the same conduct can be analyzed under both Article 81 and Article 82. It would be rather strange if we concluded that a particular form of conduct is not anti-competitive under Article 81, but infringes Article 82, with the only explanation for that divergence being that we cannot work out how to take the pro-competitive aspects into account under Article 82.

For reasons of consistency, the analytical framework for reviewing efficiencies under Article 82 should not differ much from those used under Article 81 and the Merger Regulation. In particular, I consider that it is for the dominant company to demonstrate that the following conditions are fulfilled: Firstly, the claimed efficiencies should be realized or be likely to be realized as a result of the conduct concerned. Secondly, the efficiencies should be "conduct specific"—the unilateral conduct should be indispensable to realize these efficiencies. Thirdly, the efficiencies should outweigh the negative effects of the conduct concerned. This means that we balance the pro- and anti-competitive effect of the conduct and ensure that, in the final analysis, consumers are not harmed by the conduct. Under Article 81(3) there must be a pass on to consumers.[15] I think that this should also be the case under Article 82.

Last—but in the Article 82 context certainly not the least—the well-known condition for applying Article 81(3), that competition in respect of a substantial part of the products concerned not to be eliminated,[16] must also be respected when applying Article 82. Therefore, there is a level of market power where efficiencies can no longer prevail over the long-term interest of protecting competition in the market.

Let us not, however, forget that there are numerous types of abusive conduct where there are no efficiencies at all. One re-

15. *See* EC Treaty, *supra* note 1, art. 81(3), O.J. C 325/33, at 65 (2002) (requiring that exempted agreements must give consumers "a fair share of the resulting benefit").

16. *Id.*

cent example in Europe is the *AstraZeneca* case.[17] The methods applied by AstraZeneca to misuse the patent system in that case were certainly not motivated by efficiency considerations.[18]

VI. *CONCLUDING REMARKS*

What I have summarized today is our search for sensible "rules" that would enable us to reach preliminary conclusions about when conduct may exclude competition, yet at the same time allow companies to know when they are on safe ground. Such an approach would have the advantage of being based on solid economic thinking while at the same time giving clear indications to companies and maintaining workable enforcement rules. This is of course only a first step. We intend to go on and review other categories of abuse.

I sincerely hope you will all participate in the wide discussion that we want to have on this review, with industry as well as legal and economic experts—and, of course, the other antitrust authorities including here in the United States. Thank you for your attention.

17. AstraZeneca v. Commission, Case T-321/05 (CFI June 15, 2005) (not yet reported).

18. *See* Press Release, European Commission, Competition: Commission Fines AstraZeneca €60 Million for Misusing Patent System to Delay Market Entry of Competing Generic Drugs (June 15, 2005).